

IMPORTANT: *This is a generic example of a contractor demonstration request letter. You must adapt its contents to your unique contractor environment.*

Office Symbol

Address Contractor

SUBJECT: Review of the Material Management and Accounting System (MMAS)

Dear Contractor:

As you are aware, the MMAS clause at DFARS 252.242-7004 requires contractors to assess their MMAS, conform to the ten standards contained therein, maintain their MMAS, and disclose and demonstrate it to the ACO. In conjunction with the cognizant contract audit office, we are preparing to evaluate your MMAS as required by DFARS 242.72. This evaluation will include determining compliance with the ten standards and the adequacy of related internal controls. Therefore, we request your cooperation in disclosing and demonstrating your current MMAS in a timely manner.

We intend to rely on your internal and external audit work wherever practical. Therefore, it will be to the advantage of all concerned if you provide a complete and comprehensive demonstration including all documentation supporting compliance with the standards.

According to the clause at DFARS 252.242-7004, for a *disclosure* to be considered adequate, the contractor must provide documentation which:

1. Accurately describes those policies, procedures, and practices the contractor currently uses in its MMAS and
2. Provides sufficient detail for the government to reasonably make an informed judgment regarding the adequacy of the MMAS.

Further, the clause states that for a *demonstration* to be considered adequate, the contractor must provide:

1. Sufficient evidence to demonstrate the degree of compliance of its MMAS with the standards and
2. Identification of any significant deficiencies, the estimated cost impact of the deficiency, and a comprehensive corrective action plan.

We are attaching outlines of the general expectations and expectations by standard to assist you in the development of a demonstration of your MMAS. Certainly, this list may not be all inclusive depending on the specific environment; however, please incorporate all information determined to maximize overall knowledge of the system(s) in relation to the standards.

Without an adequate in-depth demonstration, we will be required to deem the material management and accounting system inadequate and may implement billing withholds to protect the government's interest.

As you are aware, our prior review of the MMAS highlighted several areas of concern. These concerns impact your ability to maintain adequate internal controls to ensure system and data integrity. As such, it is our intention to revisit those Material Management and Accounting System (MMAS) standards that were determined noncompliant or disclosed weaknesses. (Briefly summarize the areas of concern.)

Your cooperation and assistance in this review will be greatly appreciated. Attempts to evaluate and achieve compliance with DFARS 252.242-7004 will require a coordinated effort between your specialized personnel, DCMC, and DCAA, working together as a team with a common goal. It is our hope that this will be accomplished.

Name
Administrative Contracting Officer

Enclosures:

DEMONSTRATION OF MMAS

I. Expectations

1. Describe how (contractor name) develops and manages its material and how it accounts for related costs, from requirements definition through contract completion.
 - a) Use flowcharts that describe the material system and include all significant inputs, outputs, decision times, and control points.
 - b) Describe how (contractor's name) current computer environment integrates with its MMAS. Provide sufficient documentation to allow thorough understanding of the functions and relationship of the modules and all the systems that combine to define the system.
 - c) Summarize the type and extent of testing used for each process/function to determine that the system is compliant. Also specify who performed the testing.
 - d) Explain all acronyms and abbreviations.
2. Include, for each MMAS process or function, references to written policies, procedures, operation manuals, etc.
3. Identify existing controls that ensure system is operating properly and in compliance with MMAS standards.
4. Identify types of manual or automated data input into MMAS, including description of how material is:
 - a) Ordered/tracked after a purchase order is issued
 - b) Tracked/accounted for upon arrival and while in storage
 - c) Issued to work in process (WIP) and accounted for as it moves from inventory to the end product
 - d) Disposed of during contract performance and at contract completion
5. Point out when exceptions to (contractor's name) practices could occur; explain what and why
6. Identify any significant deficiencies and provide:
 - a) The estimated cost impact of the deficiency and
 - b) A comprehensive corrective action plan
7. Provide:
 - a) Organization charts within the material organization. Include names and phone numbers of primary users as points of contact during audit.
 - b) Contractor contacts (individual names and phone numbers to contact during audit).

II. Coverage of Standards

a. Standard 1:

"Have an adequate system description including policies, procedures, and operating instructions which comply with the Federal Acquisition Regulation and Defense FAR Supplement."

1. Identify job titles of the primary users within each module and within each system -- with this, identify the source of instruction used by each of the users in performing their job functions.
2. Provide **detailed** description of the function performed by each system.
3. Explain how each of the systems that make up the MMAS interrelate and interact (directly linked or download/upload of information).
4. Diagram the primary functions of each system and reference the related policies, procedures, and controls.

b. Standard 2:

"Ensure that costs of purchased and fabricated material charged or allocated to a contract are based on valid time-phased requirements as impacted by minimum/economic order quantity restrictions--

- (i) *A 98 percent bill of material accuracy and a 95 percent master production schedule accuracy are desirable as a goal in order to ensure that requirements are both valid and appropriately time-phased.*
- (ii) *If systems have accuracy levels below these, the Contractor shall demonstrate that--*
 - (A) *There is no material harm to the Government due to lower accuracy levels; and*
 - (B) *The cost to meet the accuracy goals is excessive in relation to the impact on the Government."*

1. Provide description of how material needs are determined to include,
 - The process undergone to initiate acquisition (from a system standpoint, e.g., what are the basic inputs to the system once a contract is accepted)
 - How part is ordered and tracked after purchase order is issued
 - How part is tracked and accounted for upon arrival and while in storage
 - How part is issued to work in process
 - How part is accounted for as it moves from inventory to end product disposed of during contract performance and at contract completion.
2. Document steps taken to calculate **BOM** accuracy:
 - At what level is the accuracy rating calculated (product build level, sub-assembly, components, parts?) and to what level (drawings, engineering parts list) it is traced
 - What are the factors in the calculation formula
 - ⇒ What is an error
 - ⇒ What are source documents used to generate equation
 - How are the system generated requirements tagged to the appropriate personnel for action
3. Document steps taken to calculate **MPS** accuracy:
 - At what level of the scheduling is the accuracy calculated (end product, sub-assembly, component part)?
 - What factors go into the calculation formula
 - ⇒ What is an error
 - ⇒ What are source documents used to generate equation
 - How are the system generated requirements funneled out to the appropriate personnel for action

c. Standard 3:

“Provide a mechanism to identify, report, and resolve system control weaknesses and manual overrides. Systems should identify operational exceptions such as excess/residual inventory as soon as known.”

1. Identify the major internal controls and reports within each module to identify and resolve system weaknesses or errors (e.g., scrap, rework, lost/found parts that result in excess/shortages of material).
2. Identify the controls and reports within each module that allow for and document manual overrides (this enables managerial oversight for manual inputs).
3. Provide specific examples within each module of previously identified system disconnects and how they were resolved (identify any data that is fed from one system but not accurately received into the other).

d. Standard 4:

“Provide audit trails and maintain records (manual and those in machine readable form) necessary to evaluate system logic and to verify through transaction testing that the system is operating as desired.”

1. Provide a narrative and/or diagram, i.e., audit trail, showing the flow of parts through modules of the system.
2. Use actual transactions and show the flow of the material through the system from beginning to end (show routine and non-routine entries, e.g., material transfers between contracts due to schedule changes, etc.).

e. Standard 5:

“Establish and maintain adequate levels of record accuracy, and include reconciliation of recorded inventory quantities to physical inventory by part number on a periodic basis. A 95 percent accuracy level is desirable. If systems have an accuracy level below 95 percent, the contractor shall demonstrate that --

- (i) *There is no material harm to the government due to lower accuracy levels; and*
- (ii) *The cost to meet the accuracy goal is excessive in relation to the impact on the government.*

1. Is there contract specific material? If so, how is contract specific material stored and identified for use only on that contract?
2. In general, is material specifically ordered with a designation for commercial or military?
3. What percent of material is strictly military?
4. Are some commercial and military parts unique? If so, is the material stored separately? How is this identified at requisition point within the system?
5. What percent of material is common?
6. Provide those policies and procedures that outline methods of maintaining inventory accuracy and correct inaccuracies.
7. Provide names of individuals who supervise the inventory control process within each material crib.
8. Provide recent reports that report cycle count results for each of the cribs.
9. Provide details of the required action and controls to resolve inventory level errors identified during cycle counts.

f. Standard 6:

“Provide detailed descriptions of circumstances which will result in manual or system generated transfers of parts.”

1. Do material transfers occur? If so,
 - Provide policies and procedures that define the reasons for and controls for transfers.
 - What is dollar value of transfers in prior year?
 - Utilize system screens to trace a material transfer from the point of origin to the transfer of cost.

g. Standard 7:

“Maintain a consistent, equitable, and unbiased logic for costing of material transactions--

- (i) *The contractor shall maintain and disclose a written policy describing the transfer methodologies.*

- (ii) *The costing methodology may be standard or actual cost, or any of the inventory costing methods in FAR 30.411-50(b). Consistency shall be maintained across all contract and customer types, and from accounting period to accounting period for initial charging and transfer charging.*
- (iii) *The system should transfer parts and associated costs within the same billing period. In the few circumstances where this may not be appropriate, the contractor may use a loan/payback technique only if approved by the administrative contracting officer. When the technique is used, the contractor shall have controls to ensure-*
 - (A) *Parts are paid back expeditiously;*
 - (B) *Procedures and controls are in place to correct any overbilling that might occur;*
 - (C) *Monthly, at a minimum, identification of the borrowing contract and the date the part was borrowed; and*
 - (D) *The cost of the replacement part is charged to the borrowing contract.*

1. If there are material transfers between contracts, is the transfer of the cost being done in the same billing period as the actual part transfer?
2. What checks are in place to assure costs are allocated in the appropriate period?
3. Is the loan/payback method used to transfer parts? If so, provide policies, procedures, reasons for use of this method.
4. Provide assurances that paybacks are made expeditiously and that overbilling does not occur.
5. Utilize system screens to trace a loan/payback transaction from the point of origin to the repayment.

h. Standard 8:

“Where allocations from common inventory accounts are used, have controls in addition to those in paragraphs (f)(2) and (7) of this clause to ensure that--

- (i) Reallocations and any credit due are processed no less frequently than the routine billing cycle;*
- (ii) Inventories retained for requirements which are not under contract are not allocated to contracts; and*
- (iii) Algorithms are maintained based on valid and current data.*

1. Explain the soft-pegging and/or hard-pegging methodologies.
2. Explain the inventory allocation method/calculation used to allocate common inventory.
3. Demonstrate processing of credits within one billing cycle.
4. Identify cost records which specify contracts with credits due.
5. Demonstrate how obsolete and contract specific inventory are kept out of the allocation process when costing common inventory to contracts.

i. Standard 9:

“Notwithstanding FAR 45.505-3(f)(1)(ii), have adequate controls to ensure that physically commingled inventories that may include material for which costs are charged or allocated to fixed-price, cost-reimbursement, and commercial contracts do not compromise requirements of any of the standards in paragraphs (f)(1) through (8) of this clause. Government furnished material shall not be--

- (i) Physically commingled with other material; or*
- (ii) Used on commercial work.*

1. Approximately what percent of inventory for cost reimbursement fixed price, and commercial contracts is commingled?
2. Is government furnished material commingled with other inventory and what controls are in place to assure proper cost allocation between fixed-price, cost-reimbursement, and commercial contracts.

j. Standard 10:

“Be subjected to periodic internal audits to ensure compliance with established policies and procedures.

1. Provide internal audit’s yearly audit plan and plans for future oversight.
2. Disclose previous system reviews, including reports, working papers, and follow-up actions.
3. List completed audits and applicable reports.
4. Identify any monitoring function performed within a material organization.